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Deutsche Bank's response to the Committee on Payments and Market Infrastructures' consultation on "correspondent banking".

Dear Sir or Madam,

Deutsche Bank welcomes the opportunity to comment on the Committee on Payments and Market Infrastructures' (CPMI's) consultation on correspondent banking.

We recognise many of the trends highlighted in the consultation and agree with CPMI that many banks are de-risking operations as a result of the post-crisis regulatory and business environment. A decline in correspondent bank services serves to reduce financial inclusion and diminish access to cost-effective global transaction services for many markets, institutions, and investors. Enhanced Anti Financial Crime (AFC) requirements have significantly increased the costs of correspondent banking activities, especially with high-risk locations and counterparties as a result of correspondent banking being driven by maintaining a global network and associated relationships. Ultimately, the increased costs and perceived high risk of correspondent banking results in a more proactive review of such businesses to ensure the trust and safety of the operating model for the benefit of all nodes in the network.

The lack of a global standardised definition of correspondent banking has exacerbated the issues associated with enhanced AFC requirements. National regulators passing legislation independently without coordination with other jurisdictions has raised concerns that the provision of any cross-border financial services through an intermediary with another financial institution (apart from FX or Money Market transactions) may amount to a correspondent banking relationship and subsequently introduce additional cost and complexity, through greater due diligence requirements, rendering the business less economically attractive.

The Financial Stability Board (FSB) report on correspondent banking from 6 November emphasised the need for regulators to clarify regulatory expectations and agree to a uniform approach with respect to the performance of due diligence in high risk jurisdictions. Deutsche Bank supports the development of an equivalence standard across jurisdictions to decrease the uncertainty around regulatory requirements, especially regarding high risk locations.

We support the recommendations that CPMI proposes to improve the correspondent banking environment and see merit concentrating on the following areas:

- **KYC Utilities must be secure and reliable:** With the right governance and operational structure, KYC utilities (e.g. SWIFT Registry, KYC.com) can assist the correspondent banking environment and ensure there are central utilities that can store reliable KYC information. In order for these registries to become universally beneficial, registries must



be developed that are considered secure and reliable, and all correspondent banks (and beyond) will have to participate.

- **LEIs should be phased in over time:** The increased use of Legal Entity Identifiers (LEIs) will benefit both regulators and industry participants through simplified and standardised counterparty data and greater transparency. However, it is not practical to introduce these requirements over the short or medium term because of the significant costs and complexities associated with adoption, especially if implementation is considered within the scope of today's ISO Standard 17442.
- **Information sharing:** The use of KYC registries to share key KYC information is a welcome initiative that has the potential to reduce costs, but the current lack of clarity and certainty surrounding data privacy from regulatory standard setters gives rise to potential unacceptable levels of risk. We agree that here is a need for regulatory standard setters (i.e. FATF, AMLEG) to determine global minimum levels of due diligence that correspondent banks should carry out as relates to KYC on client's clients and RMAs.
- **Transition to a serial message approach:** A shift from a 202 Cov message type to a serial 103 message approach would lead to greater security and certainty and ensure the full payer and payee details are passed throughout the correspondent banking chain.

Please do not hesitate to contact us if you have questions or wish to discuss any of these comments further.

Yours sincerely,

Daniel Trinder
Global Head of Regulatory Policy



Annex I: The Use of Know Your Customer (KYC) Utilities

We strongly support the use of KYC utilities. The creation of a harmonised KYC utilities standard is integral to the success of such tools and should focus on the required data fields, frequency of data updates, and data quality controls. In order to enable banks to follow a risk based approach in their internal due diligence evaluations, local regulatory requirements and additional data field requirements should also be considered. Further global coordination is needed to establish minimum requirements and standards for KYC utilities. As a result of different local regulatory approaches, there is a risk of fragmentation in KYC utilities. An industry body, such as the Wolfsberg group, would be well placed to create such a global standard, which could in turn be endorsed by regulators.

Along with the creation of a harmonised standard, the regular auditing of KYC data by home authorities associated with their home banks is also required. With the reliability of data central to the KYC process, the validity of KYC documentation requires checks by the utility provider in order to establish the KYC utility as a trusted data source. A local regulatory audit of the data related to their home banks would provide comfort that the data available was acceptable (banks would still need to assess their own view of the risk of doing business with that counterparty).

The use of KYC utilities for corporates needs to be central to the review of correspondent banking. Corporate payments need to be considered, as these open up banks to similar data and regulatory risks, and are equally critical to the functioning of cross border payments business. There are a number of ways to achieve this. Whilst it would make sense for the registries to incorporate corporate related KYC information, another option would be for KYC utilities currently focused on corporates to update their product offerings to cover correspondent banking and related requirements. This, however, has to be closely aligned with any further evolution of the LEI in order to avoid double-developments.

Annex II: Use of Legal Entity Identifier (LEI)

We support the FSB objective to incorporate the use of LEIs across all financial counterparties and all key transaction types. For payments, the introduction of a single LEI reference (if introduced effectively over the long term) will aid the ability to identify counterparties and analyse the nature and types of business within the payment transaction flows. We are concerned, however, that in the short to medium term, there are significant complexities associated with adoption, especially if implementation is considered within the scope of today's ISO standard.

In addition to the identification of a legal entity, the main benefit of LEIs in payments is where they could be used to identify the nature, line of the business and the industry of the entity. The implementation of the LEI would provide a valuable tool that could be used to analyse the underlying business of the different parties in the payment chain. Hence, it would complement and support Anti Money Laundering (AML) efforts, and assist correspondent banks better understand the co-relation between originators and receivers. Therefore, for the introduction of LEIs to be most effective, we would suggest a review be performed of the current, underlying structure of ISO Standard 17442.

The payments industry is in the initial stages of transitioning to the ISO 20022 XML financial messaging standard for transactions, a process that is still several years from completion. As LEI adoption will be factored into messaging infrastructure once the shift to ISO 20022 is complete, it is not sensible to rush LEI implementation as we transition away from current SWIFT MT payments formats. To avoid the duplication of efforts we would recommend that



LEI is adopted as part of the ISO 20022 roll out, where its implementation can be planned more effectively.

SWIFT BIC codes are the predominant identifier that correspondent banks use to recognise one another. This identifier is effective for payment purposes and should continue to be used (a BIC provides for more pertinent information, such as routing data, when making payments compared the information currently available with LEIs).

The introduction of LEIs could provide greater transparency relating to payment initiators or beneficiaries, such as corporates, rather than correspondent banks. However, presently such initiators or beneficiaries do not broadly utilise LEI codes (unless they trade derivatives). With today's level of adoption, the benefits to correspondent banks would be minimal. We recognise that global regulators continue to push for the adoption of LEIs into new products such as securities, and this will ultimately benefit correspondent banking and payments when LEIs are adopted here too.

Our recommendation therefore is that the use of LEIs in payments should be adopted over a longer period of time, in line with the adoption of XML.

Annex III: Information Sharing

We welcome focus on information sharing, and recognise the various challenges and opportunities highlighted in the paper. There is a need for regulators and the industry to work together on this area, and determine key priorities for focus.

There are issues relating to the sharing of data on a cross border basis. Banks that participate in cross border correspondent payments require flexibility in their ability to share data between their branches and subsidiaries both to manage risks effectively and to comply with local regulations. However, there are some jurisdictions where data cannot be shared on a cross border basis, or where restrictions are placed on the use of such data (often to protect underlying investors or parties). Although understandable, data restrictions make complying with regulatory requirements elsewhere and risk management difficult for banks, which can reduce the appetite to operate in certain jurisdictions. The BIS should prioritise focusing on determining standards for data sharing and on what basis. This might allay certain jurisdictions' concerns if such standards provided a clear basis that balance the needs of banks to facilitate business and manage their risks, with the needs of institutional and retail data privacy requirements.

In developing new central registries or databases there are outstanding and complex issues that must be considered. These are mainly caused by a lack of clarity on how they will operate, who will have access rights, and who will be responsible for the maintenance of the data quality and system infrastructure. Such databases would likely hold sensitive data that would require high level system safeguards to ensure privacy and security of data. Finally, work is needed to develop understanding of how these information sharing initiatives would interface with the use of KYC utilities as there would likely be some overlap of data.

Annex IV: Payment Message Flows

If the recommendation in the paper to move to a serial message approach within the industry is undertaken, we broadly support such measures (103 message type rather than a 202 Cov message type). In addition to improved security and certainty in the payment chain, market concerns related to significant latency within the system caused by this approach could be mitigated through the introduction of new technologies that will help reduce the time lag for cross border payments. This process could be reinforced by a global standard for serial messages.



One concern the industry would have moving to a serial approach relates to cross border flows that pass via payment clearing houses, and whether there would be a delay in payment settlements as a result of different time zones and opening times of market infrastructure. We believe such concerns could be allayed if clearing infrastructures were to extend their opening and cut off times to facilitate payments over a longer period during the day, thus providing a greater opportunity for cross border payment flows to be processed. We note for example that in the U.S., Fedwire and CHiPs extended their opening hours by opening at 9 pm on value date -1. We would encourage other key clearing systems to adopt similar approaches.

We believe that moving to a serial approach should be done in stages. Setting up a combined serial and cover payment approach would be a good interim step for the following reasons:

- Originating banks would use the MT103 to ensure the beneficiary bank has the information needed even when there is no direct clearing relationship between them.
- The correspondent bank would use the same MT103 to pass the information onto the beneficiary, ensuring the necessary information is present in the payment chain.
- A combined approach would also allow the correspondent bank flexibility to send information, where appropriate, using 202 Cov to another bank in the same jurisdiction.

Any shift to serial messaging would cause a fundamental change in current market practice. Therefore, sufficient time would be required to fully assess all impacts, educate the market, and ensure technical and process changes could be made by banks and market infrastructures.